STATE OF NEVADA
DEPARTMENT OF BUSINESS AND INDUSTRY
REAL ESTATE DIVISION
ADVISORY OPINION

Subject:		
Is the approval of units' owners required for expenditure of operating funds on capital projects?	Advisory No.	**12-02-116**
	Issued By:	Real Estate Division
	Amends/ Supersedes	N/A
Reference(s): NRS 116.3114; Nevada Common-Interest Community Manual, Chapter 10 - Fiscal Matters; NRS 116.31151		Effective Date: December 12, 2011

QUESTION:

Is the approval of units' owners required for expenditure of operating funds on capital projects?

ANALYSIS OF THE ISSUE:

"Capital improvement" is not defined in Chapter 116. Capital improvement funds, however, are funds designated for the *acquisition* or *construction* of new common area components. Examples are the construction of a new clubhouse or the purchase of adjacent land for a park. After the new components are acquired, they may need to be included in the reserve study for the future repair or replacement.

The association operates under a fiscal plan called an annual budget which lists planned revenues and expenses for a given year. The budget determines what types of costs are expected to be incurred and when. The budget is the basis for the calculation of the current year assessments paid by all homeowners to fund the association.

The goal for budget planning is to determine as closely as possible how much money is needed to fulfill the association's needs and assess the owners just the right amount to ensure that funds are available. The budget sets forth the plan for the association's operation.

Surplus funds are funds remaining after payment of liabilities for common expenses and reserves. NRS 116.3114 addresses surplus funds: "Unless otherwise provided in the declaration, any surplus funds of the association remaining after payment of or provision for common expenses and any prepayment of reserves must be paid to the units' owners in proportion to their liabilities for common expenses or credited to them to reduce their future assessments for common expenses."

The statements in this advisory opinion represent the views of the Division and its general interpretation of the provisions addressed. It is issued to assist those involved with common interest communities with questions that arise frequently. It is not a rule, regulation, or final legal determination. The facts in a specific case could cause a different outcome.

The law addresses surplus funds by first deferring to the association's own governing documents. If the governing documents address the dispensing of surplus funds, then the association would follow those instructions. The governing documents may include language that sets forth a spending cap on capital projects without unit owner's approval (such as up to a certain percentage or dollar amount), or may specifically state whether capital projects require approval of unit's owners.

If the governing documents are silent, the statue provides two options regarding surplus funds:

- They may be refunded to the units' owners in proportion to their liabilities for common expenses, or
- They may be credited to them to reduce their future assessments for common expenses.

ADVISORY CONCLUSION:

NRS 116.3114 requires that the association first look to its governing documents to determine the method that surplus funds could be allocated. The association's governing documents should determine whether a spending cap on capital projects without units' owners' approval exists, or whether capital projects require the approval of units' owners at all.

Otherwise, NRS 116.3114 requires that surplus funds be paid to the units' owners in proportion to their liabilities for common expenses or credited to them to reduce their future assessments for common expenses.

The executive board may adopt the funding of capital improvement expenditure in the annual budget. The budget may utilize surplus funds to fund capital improvements in the adopted budget. In that way, the surplus funds would be credited to each unit owner in proportion to their liabilities for common expenses, thereby reducing their future assessment for the additional common expense.

Once adopted by the executive board of an association, the budget is submitted to the membership for ratification pursuant to NRS 116.31151. If unit owners do not agree to the capital improvements as adopted by the board and presented to the unit owners to ratify, the unit owners would have the option to not ratify the budget.